No. 11,115

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

AMERICAN BOX SHOOK EXPORT ASSOCIATION (a corporation),

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REPLY BRIEF OF PETITIONER ON REVIEW.

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THE JURISDICTION OF THIS COURT IS ADMITTED.

The Brief heretofore filed by respondent clarifies the issues at least to the extent that the respondent states his agreement that the question presented to this Court is one of law (Res. Brief, p. 15), and, therefore, a question upon which the jurisdiction of this Court is unquestioned.

THE QUESTION FOR DETERMINATION BY THIS COURT IS: DOES A FULLY EXECUTED ORAL AGREEMENT FOR THE PURCHASE AND SALE OF COMMODITIES CONTAINING A PROVISION THAT A PORTION OF THE PURCHASE PRICE SHALL BE PAID AFTER RESALE OF THE COMMODITIES BY THE PURCHASER CONSTITUTE A VALID AND ENFORCEABLE AGREEMENT AND THEREFORE A FIXED LIABILITY OF THE PURCHASER?

There is no dispute between the parties as to the primary question, that question being: "Were the contracts between the Association and its members valid and enforceable agreements as the taxpayer asserts, or mere unenforceable 'arrangements,' as is the position of the respondent?"

In its Statement, on page 4 of Respondent's Brief, the respondent restates the fact of the existence of "an understanding between the taxpayer and its members that any amounts received in excess of actual cost, with the exception of amounts placed in reserve for anticipated claims is to be returned to them".

Respondent argues that the agreements between the taxpayer and its members were not a "fixed liability" of the taxpayer. To quote the respondent's own language, the respondent states, at the bottom of page 5 and the top of page 6 of its Brief, that the Tax Court found that there was such an understanding, but held that "since it was merely an informal arrangement not contained in any express written contract or in the articles of incorporation or by-laws, such understanding did not amount to the fixed liability required before a taxpayer may be relieved of tax on sums distributed".

The question then may be restated:

> Did the executed oral agreements between petitioner and its members create "a fixed liability" on the petitioner association to return to its members all sums received by it in excess of costs of operation?

Considering for a moment the statement of respondent, it would seem clear that a valid and enforceable agreement need not be contained in an express written contract, nor does its enforceability or validity depend upon its inclusion within articles of incorporation or by-laws. It is true that a contract may be expressed in writing and may be contained in articles of incorporation or by-laws, but a contract need not be so expressed.

It may be a slight over simplification to say that the case at Bar results from the tax collector's natural prejudice against oral agreements, yet the whole burden of the respondent's argument is, to use his own language, that there was not "an express written contract". The witnesses for Petitioner referred to the terms of the purchase and sales contracts between Petitioner and its members variously as "an understanding", "an arrangement", "an agreement" and as "a plan of operation". The Tax Court referred to it only as an "understanding", though the respondent in his Brief also uses the word "arrangement". Whatever term may be used to denote the agreement, the evidence of the terms of the agreement is clear and includes a written memorandum sufficient to indicate the general terms of the agreement. That there is no dispute as to the terms of the agreement is made clear from the Tax Court's own Finding of Fact. The

memorandum contains one phrase "upon action of the organization" which is not quite clear and therefore is subject to explanation. The meaning of that somewhat ambiguous phrase was made clear by the testimony. There were then all of the elements of an executed oral agreement fully understood by all of the parties and carried out by all of the parties within the taxable year.

Respondent's Summary of Argument (Resp. Brief, p. 6) suggests that the "conclusion" of the Tax Court is buttressed by five stated propositions. We will consider them in the order in which they are stated in the Summary of Argument.

1. The first is that the evidence shows that no distributions were, or could be, made without action of the Directors. In the Opening Brief of the Petitioners, we quoted the evidence with respect to the meaning of the phrase "upon action of the organization". (Brief of Petitioners, pp. 14, 15, 18 and 19.) That evidence, and there is no conflicting evidence, shows clearly that the only question to be "acted upon" by the Director members of the Association was the amount of funds necessary to retain to cover possible future contingencies. All of the rest of the money was to be distributed.

2. The second of the Tax Court's "conclusions", as stated in the Summary of Argument, was that there was nothing to prevent the taxpayer's directors from voting regular dividends. There are two answers to this "conclusion": 1st, the contracts of purchase and sale between the Association and its members pre-

cluded the possibility of any "profits" to distribute as dividends; and, 2nd, none were ever declared.

3. The third statement is to the effect that the taxpayer had not adhered to the understanding in practice—a statement directly opposed to all of the evidence which shows beyond question that the taxpayer did distribute all of the funds in its treasury except only that amount which the Director members felt should be temporarily withheld to cover possible future claims.

4. The fact that the taxpayer Association was formed under the General Corporation Laws of the State of California rather than under the specific statutes referring to nonprofit cooperative associations, is relied upon by respondent as a reason for the Tax Court's refusal to recognize the agreements between the taxpayer Association and its members as "fixed liabilities" of the taxpayer Association. It is not clear to us how that fact can have any bearing at all upon the validity of the taxpayer Association's agreements with its members.

5. The fifth "conclusion" is that the Association intended to, and did, engage in export trade for a profit as any other business corporation would have done. The evidence is that the corporation did act in effect as the export department of the various member firms and was no more than an agency used by the member firms to conduct their export trade under agreements which effectively denied to the corporation even the possibility of making a returnable profit.

AN OVERPAYMENT OF TAX GIVES THE TAXPAYER A RIGHT TO REIMBURSEMENT BY THE TAXING AUTHORITIES AND DOES NOT CONSTITUTE THE BASIS FOR ASSESSMENT OF ADDITIONAL OVERPAYMENT BY RESPONDENT.

In that portion of its Brief entitled "Argument", respondent refers to the fact that the tax return filed by the corporation did not claim complete exemption from taxation, apparently on the theory that this initial mistake on the part of taxpayer Association's bookkeepers in some way prejudices the taxpayer's claim to be free of tax. The Tax Court made no such error, and that Court properly stated the issue in the case at Bar as to whether "any of the amounts received by the petitioner for the year in question are taxable to it as income". (Rec. p. 19.) The taxpayer does claim that all of its income belonged to its members, or stated otherwise, that it had no taxable income. Any tax paid by it to the respondent was paid because respondent had ruled that taxpayer was not exempt. If, as we believe, taxpayer has paid a tax improperly assessed against it, then it has a right to file a proper claim for refund and receive reimbursement from the respondent. We see no justification for respondent's argument that, because the taxpayer has actually paid a tax, which it need not have paid, it should now pay a further tax.

The question presented to the Tax Court, and which that Court stated to be the primary question before it, was whether or not the taxpayer Association had any taxable income. That question depends upon the validity or invalidity of its agreements with its members and not upon whether or not the taxpayer made an error in filing its income tax return and in paying to

respondent a tax which should not have been paid and which may, therefore, be recovered back by the taxpayer.

THE DECISION OF THE TAX COURT IS NOT FOUNDED UPON ITS FINDINGS OF FACT BUT IS IN OPPOSITION AND CONTRARY TO THE ONE FINDING OF THE TAX COURT UPON THE SUBJECT AND THE RESPONDENT IS BOUND BY THE FINDINGS OF FACT OF THE TAX COURT.

In its Brief, the Petitioner argued that the decision of the Tax Court was without support in its Findings of Fact. In answer to that proposition, the respondent argues that the Court should consider the Decision as though it were labelled "Findings of Fact", and as authority refers to the decision of this Court in *California Iron Yards Co. v. Commissioner,* 45 Fed. (2d) 514, decided in 1931.

In the case of *Kelleher v. Commissioner of Internal Revenue,* decided by this Court on January 24, 1938, and reported in 94 Fed. (2d) 294, this Court stated at page 295:

> "These were questions of fact, as to which the Board should have made, but did not make, specific findings. Such findings are necessary to a decision of the case and should be made by the Board, not by this Court. In reviewing decisions of the Board, we are not authorized to make findings of fact. Our review is limited to questions of law."

The Court, in effect, thereby overruled its decision in *California Iron Yards Company* case, as appears more clearly in the first sentence of the dissent in the opinion of the *Kelleher* case in which the dissenting Judge

took the same view now taken by counsel for respondent.

In the Brief of Petitioner, we quoted from the decision of the Supreme Court of the United States in the case of *Dobson v. Commissioner,* 320 U. S. 489, the following language from page 502:

> "It is, of course, the duty of the tax court to distinguish with clarity between what it finds as fact and what conclusions it reaches on the law."

It would, therefore, seem clear that the Supreme Court of the United States has thus adopted the rule of this Court as that rule is stated in the *Kelleher* case. The Tax Court, in the case at Bar, clearly distinguished between what it found as fact and its conclusions by labelling its findings of fact as such.

We submit that the decision of the Tax Court is without support in the findings of that Court or in the evidence and must, therefore, be reversed.

Dated, San Francisco,
December 17, 1945.

Respectfully submitted,
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